HOUSE BUDGET COMMITTEE

Democratic Caucus

The Honorable John M. Spratt Jr. ■ Ranking Democratic Member

B-71 Cannon HOB ■ Washington, DC 20515 ■ 202-226-7200 ■ www.house.gov/budget_democrats

July 22, 2004

Summer Recess Package on the Budget

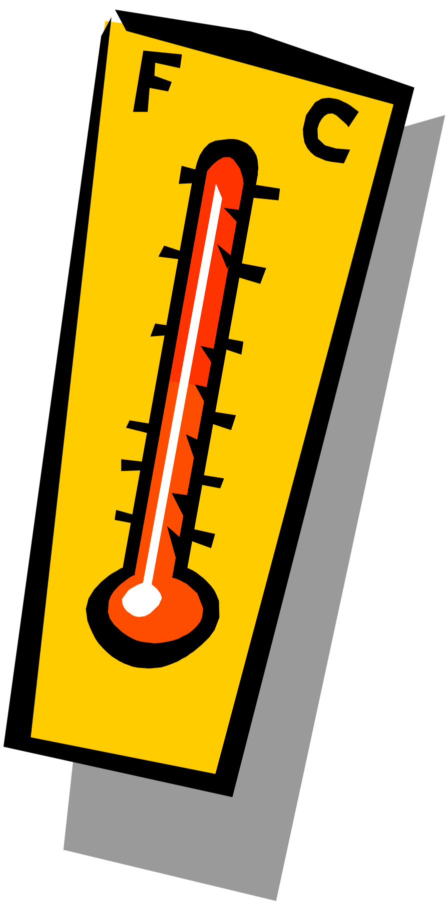
Dear Democratic Colleague:

Attached is a package of budget materials; I hope it will be helpful to you during the Summer District Work Period. Do not hesitate to contact me or the Budget Committee Democratic staff with any questions.

Sincerely,
/s
John M. Spratt, Jr.
Ranking Democratic Member

It’s Summer!

Temperatures are Rising, and So are Republican Budget Deficits



House Budget Committee
Democratic Staff

Summer Recess
Package

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Summer Recess Package on the Budget

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July 22, 2004

Fiscal Year 2005 Budget Update

Facing Record Deficit, Administration Delays Release of Mid-Session Review of Budget — Federal law requires that the *Mid-Session Review* of the budget be released by July 15, but the Administration missed this deadline and still has not released the document. The *Mid-Session Review* is expected to contain another record deficit for 2004, even though the Administration will likely attempt to characterize that record deficit as representing "improvement." Deficit figures included in the *Mid-Session Review* also will likely omit the cost of a number of items with large price tags, meaning that deficits are likely to be even larger than the *Mid-Session Review* will indicate. (For more on this topic, see *The Mystery of the Missing Mid-Session Review*, page 3)

Republicans Fail to Pass Budget Resolution Conference Report; Budget Process Broken — Federal law requires that the Congress pass a budget resolution conference report by April 15. The Republican failure to pass a budget resolution conference report this year marks the first time in history that a budget conference report has not been agreed to when the same party controls both houses of Congress and the White House. Republicans also have abandoned the long-term budget window that would show the full consequences of their failing policies: the customary ten-year window has been reduced first to five years, and recently to only one year. Even though Republicans have no budget to enforce, they nevertheless brought a misguided budget enforcement measure to the House floor — and then were unable to pass it. (For more on this topic, see *The Mystery of the Missing Mid-Session Review*, page 3)

Record Deficits Require Another Debt Ceiling Increase — The Bush Administration inherited a $5.6 trillion surplus in 2001, which has become a $2.9 trillion deficit — an $8.5 trillion swing. Instead of bringing forward plans to return the budget to balance, Republicans suggest more of the same misplaced priorities: large tax cuts for those who need them least and spending cuts to vital services. As a result of their policies, Republicans need another increase in the debt limit — the third debt ceiling increase in three years. (For more on this topic, see *Republicans Need to Raise the Debt Limit — Again*, page 5)

Full War Costs Drive Deficits Even Higher — Costs for ongoing military operations in Iraq and Afghanistan continue to increase, but the Administration is unwilling to acknowledge the full cost of these efforts. Just this week the Government Accountability Office released a report documenting that funding in certain Defense Department accounts is expected to fall short this year by $12.3 billion. As spending for the war rises, the deficit outlook deteriorates even further than Republicans admit. (For more on this topic, see *Spratt Statement on New GAO Report Showing $12.3 Billion Shortfall for War*, page 6)

Misplaced Priorities Lead to Sharp Cuts — Republican budgets make room for tax cuts and continue to waste taxpayer dollars through higher interest payments on the federal debt. At the same time, Republican budgets fail to fund adequately important domestic programs and homeland security needs. Misplaced priorities have already resulted in funding shortfalls in both the Interior and Homeland Security appropriations bills for 2005, and the Administration is planning even sharper cuts for 2006. (For more on this topic, see *2005 Appropriations: Republican Priority on Tax Cuts Will Harm Domestic Services*, page 8, and *Administration Confirms Its Plan to Cut Many Services Deeply in 2006*, page 11)

Economy Slow to Rebound — Middle-class Americans and the economy still struggle after three rounds of tax cuts and three years of Republican control in Washington. The Bush Administration has failed to generate a meaningful recovery for an economy that slumped on its watch, and nearly two million private-sector jobs have been lost since President Bush took office. (For more on this topic, see *Inflation and Stagnant Wages Leave Low- and Middle-Income Workers Behind*, page 15)

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July 15, 2004

The Mystery of the Missing Mid-Session Review

Though in control of Congress and the White House, Republicans cannot get their act together on the budget. Republicans have failed to approve a budget resolution conference report, pass legislation to raise the debt ceiling, enact meaningful budget enforcement measures, or complete any of the appropriations bills for 2005. Now, the White House has announced that the *Mid-Session Review*, a statutorily required report to update Congress and the public on the status of the nation's fiscal health, is not being delivered on time.

Yet Another Piece of Unfinished Business

For the first time ever when the same party controls the White House, the Senate, and the House of Representatives, Republicans are unable to agree on a budget resolution. Without a blueprint for funding and revenue priorities, spending and tax cut measures cannot be considered within the context of an overall fiscal framework.

For the third time in three years, Republicans need to increase the debt limit. Last year, they enacted the largest debt limit increase in history: $984 billion. In 2002, they raised the debt limit by $450 billion. Now, they need another $690 billion increase to keep the federal government solvent for just one more year.

Republicans are unwilling to recognize the fiscal consequences of their actions. First, Republicans tried to use the "Hastert Rule" to produce an increase in the debt limit through their budget resolution without having to take a separate vote. Then House Republicans tried to cloak the urgently needed debt limit increase in an unrelated must-

Republican Budget To Do List

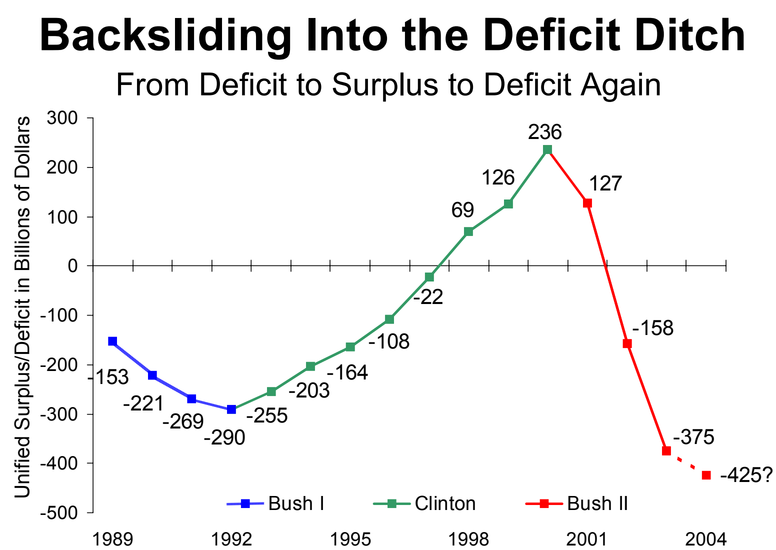
- [x] Set a new deficit record
- [ ] Deliver Mid-Session Review on time
- [ ] Pass a budget resolution conference report
- [ ] Pass a debt ceiling increase
- [ ] Pass effective PAYGO extension, spending caps
- [ ] Pass appropriations conference reports on time

pass bill. Because both attempts were unsuccessful, the federal government is likely to run up against the debt limit in September or October, according to the Treasury Department.

With no budget in place to enforce, House Republicans still brought several ill-conceived budget process reform measures to the floor for consideration last month. The lopsided Republican proposal to restrain spending without limiting tax cuts was a bad idea, and the draconian entitlement cap procedure included in some Republican amendments was even worse. Because Republicans were unwilling to compromise, they squandered the opportunity to enact meaningful, bipartisan budget process reform; instead, every major proposal was rejected, including a return to the budget rules that worked throughout the 1990s.

Why The Delay?

Although the White House may want to tout new numbers as representing fiscal improvement, the fact is the *Mid-Session Review* will set another deficit record. For that reason, the White House may release the numbers in the dead of August when Congress is not here to receive them.



Republicans Still Headed in the Wrong Direction

Republican budgetary policies have landed on the American economy with a thud. Inherited surpluses have become historic deficits under Republican leadership, and failed economic policy has resulted in a sluggish recovery and enormous job losses.

Because of their unbalanced tax cuts, Republican budgets require deep cuts to important domestic priorities, not just for 2005, but for 2006 and beyond. Republican policies continue to send the country in the wrong direction.

Likely to Be Incomplete When It Finally Arrives

Even while showing record deficits, new figures in the *Mid-Session Review* will likely omit some key items, particularly in the estimates of future deficits. In February, the Administration predicted large deficits, but those estimates failed to include the costs of items such as alternative minimum tax relief, the war in Iraq and Afghanistan beyond 2004, expiring tax provisions, the continuing defense buildup, and realistic discretionary funding amounts. While Democrats expect the *Mid-Session Review* numbers to set new deficit records, the Administration is still likely to leave out many items with large price tags. The actual cost of the Republicans' agenda will be much higher than they acknowledge.

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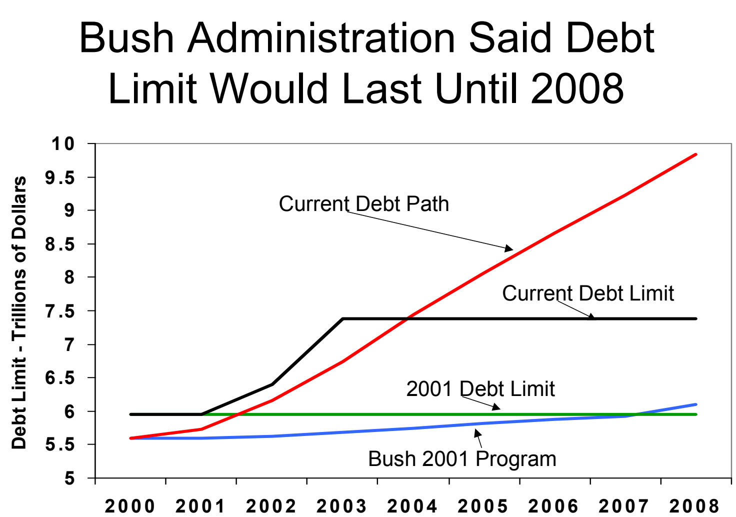
July 22, 2004

Republicans Need to Raise the Debt Limit — Again

For the third time in three years, Republicans need an emergency increase in the debt limit. Last year, they enacted the largest debt limit increase in history: $984 billion. In 2002, they raised the debt limit by $450 billion. Now, they need another $690 billion increase to keep the federal government solvent for just one more year, and time is running out. In his July 2 letter to Ranking Democratic Member John Spratt, Treasury Secretary Snow wrote, “We currently estimate that the federal government will likely brush up against the debt limit in September or October. Accordingly, it is imperative that the Congress pass legislation to increase the debt limit as soon as possible.”

Republicans are unwilling to take full responsibility for the fiscal consequences of their policies, and seek to avoid any direct vote on raising the debt limit. First, Republicans tried to use the “Hastert Rule” to produce an increase in the debt limit through their budget resolution without having to take a separate vote. But they could not agree among themselves on a budget resolution conference report. Then House Republicans tried to cloak the urgently needed debt limit increase in an unrelated must-pass bill.

When President Bush and the Republican Congress increased the debt limit by $984 billion in 2003, they achieved the largest debt limit increase in history. The $690 billion debt limit increase that is implied in the budget resolution conference report will be the third largest in history. The $450 billion that President Bush needed in 2002 was the sixth largest. So the debt limit increases needed by President Bush and the Republican Congress over the last three years constitute three of the seven largest hikes in history, totaling $2.124 trillion. That is more than the total debt accumulated by the United States from its founding through August of 1986. In the last four years of the Clinton Administration, the nation never needed a higher debt limit. That was the payoff of Democratic fiscal responsibility.



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July 21, 2004

Spratt Statement on New GAO Report Showing $12.3 Billion Shortfall for War

WASHINGTON - U.S. Rep. John Spratt (D-SC) issued the following statement on today's release of a new Government Accountability Office (GAO) report that he requested. The GAO report documents a $12.3 billion shortfall in the Defense Department's 2004 budget resulting from increased requirements to support operations in Iraq and Afghanistan.

"The GAO has issued a disturbing report. The report shows that the Department of Defense (DoD) will fall $12.3 billion short of funding operations and maintenance and military personnel this year. This is another in a long line of miscalculations connected with our deployments in Iraq mainly but also Afghanistan. The Administration under-estimated troop levels, under-estimated the tempo and cost of operations, and under-estimated the cost of logistics, maintenance, spare parts and services provided by contractors.

"GAO found that DoD has funds within other areas of the budget to partially offset the shortfall. However, it also found that the Military Services — the Army, Navy, Marine Corps, and Air Force — will be forced to defer regular operational requirements from 2004 to 2005 in order to free up funds to make up the balance. Such plans are likely to have adverse consequences for next year's budget and the readiness of our military forces.

"The House Budget Committee Democratic Staff estimates that DoD has $5 billion of resources available from supplemental and regular appropriations to fund a portion of this shortfall. This still leaves the Department $7 billion short in the last two months of fiscal year 2004. The final 2005 defense appropriations bill sets up a $25 billion emergency fund for Iraq and Afghanistan operations and makes it available immediately after enactment to cover any 2004 shortfall. The Administration has indicated that it will not use the emergency fund. Instead, it expects the services to go forward with plans to defer 2004 requirements into 2005, by delaying equipment and facility maintenance, reducing flying and ship steaming hours in support of non-deployed training, and diverting the savings to fund combat operations. This will make the deficit for 2004 look smaller, but it will constrain next year's budget and adversely affect the military readiness of our non-deployed forces during a time of war. This is bad policy and begs the question: Why does the Administration pursue it?

"The Administration seems to choose this course because if it drew down the $25 billion reserve to cover this year's shortfall, it would have to admit its miscalculations and add to a swollen deficit. This year's shortfall results from underestimating the insurgency in Iraq and the number of troops needed to put it down. More generally, it results from inadequate planning for post-war Iraq.

"The Administration has been unwilling to recognize the full cost and adequately fund operations in Iraq and Afghanistan. In February, the President requested no funds for these operations in his FY 2005 budget. In the absence of these funds, the military services would be forced to shift funds from regular appropriations to pay for operations in Iraq and Afghanistan. Three months later, as the situation worsened in Iraq, the President amended his budget to request a modest $25 billion, at most half of what will be required, to cover the shortfall in 2005. Today, it's apparent that the Department of Defense will face a much worse funding shortfall toward the end of this year than the Pentagon predicted only months ago. Yet, instead of recognizing these costs and planning to tap the additional funds the Congress is making available, the Administration plans a temporary expedient. It will cut back on other activities and further burden our military.

"This Administration has failed to budget for the war in Iraq and Afghanistan. The time is long past due for the Administration to present a full accounting of the cost of the war and to ask Congress to put up the resources needed to fund it."

# # #

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July 22, 2004

2005 Appropriations: Republican Priority on Tax Cuts Will Harm Domestic Services

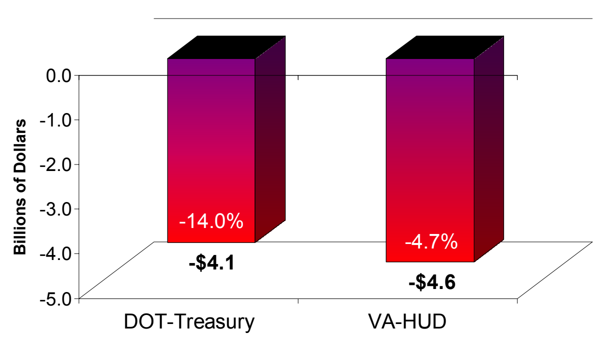
Republican Budget Resolution Cuts Domestic Spending

House Republicans passed a budget resolution that chose to make room for $55.2 billion of additional tax cuts but to shortchange spending for vital domestic services. As a result of this choice, Republicans are cutting 2005 domestic funding — all funding except for defense and international programs — by a total of $11.1 billion below the amount needed to maintain services at their 2004 levels. ***This translates into a domestic cut of $487 million below a freeze at the 2004 enacted level.***

Budget Limits Delaying Appropriations Bills

Congress will be in session for less than four more full weeks prior to the beginning of fiscal year 2005, but the House has not yet passed the three largest domestic appropriations bills, and the Senate has yet to pass 12 of the 13 appropriations bills. The House has yet to consider the bills funding the Departments of Veterans Affairs, Housing and Urban Development, and independent agencies; the Departments of Transportation and Treasury; and the Departments of Labor, Health and Human Services, and Education. The House presumably left these three funding bills — accounting for about one-third of all appropriations — until last because it is likely to have trouble passing steep cuts in programs that provide vital services.

Pending House Bills Below Amount to Maintain 2004 Services



Both the Treasury-Transportation and the VA-HUD bills are cut by more than $4 billion below the amount needed to maintain services at the 2004 level.

Cuts in Three Bills Awaiting House Consideration

The low level of funding in the budget requires appropriators to make cuts in important services, including the following cuts (although Appropriations Committee and House consideration could still shift money among programs in these three bills):

- ***Cuts HUD, EPA, NSF, and NASA*** — The Appropriations Subcommittee cut the 2005 appropriations bill for VA-HUD-Independent Agencies by $4.6 billion (4.7 percent) below the amount needed to maintain services at the 2004 level. Because the bill increases funds for veterans' health care by $1.9 billion over the 2004 enacted level, it is forced to cut funding for many other programs even more. These cuts include the Environmental Protection Agency (cut $613 million below the 2004 enacted level), the National Science Foundation (cut $111 million), the National Aeronautics and Space Administration (cut $229 million), and HUD (cut $108 million, with most programs cut by 4 percent below their 2004 enacted level).

- ***Cuts Amtrak, Air Traffic Control Improvement*** — The Appropriations Subcommittee cut the Transportation-Treasury bill by $4.1 billion (14.0 percent) below the amount needed to maintain services at the 2004 level, and by $3.0 billion below the 2004 enacted level. The cuts include Amtrak, cut by $318 million (26.1 percent) below the 2004 enacted level, and funding to improve air traffic control and airway facilities, cut $393 million (13.5 percent).

- ***Shortchanges Education, Health, and Training*** — The Appropriations Committee funded the Labor-HHS-ED bill at $1.3 billion (0.9 percent) above the amount needed to maintain current services, but because special education and Title I receive $1 billion increases, appropriators had to cut many other programs. These cuts include eliminating 23 education programs, funding No Child Left Behind Act programs at $9.5 billion short of the authorized level, cutting rural health services by nearly $60 million, and freezing or cutting funds for other child care, training, health, and education programs.

House Approves Other Painful Cuts

Although the full impact of the cuts to particular programs will not be clear until Congress completes the appropriations bills discussed above (when this document was printed, the full Appropriations Committee had yet to consider the VA-HUD and Transportation-Treasury bills), there are other troubling cuts in the bills that the House has already passed.

- ***Cuts First Responder Programs*** — The Homeland Security bill cuts funding for first responder programs at the Department of Homeland Security from $4.4 billion to $4.2 billion, a cut of $277 million below the 2004 enacted level. The bill's increase ($279 million) for grants for high-threat urban areas is offset by a larger cut ($440 million) to formula-based grants. The bill cuts funding for firefighter assistance grants by $96 million (12.9 percent) from the 2004 enacted level of $746 million. A 2003 Council on Foreign Relations study estimated $98 billion in unmet needs for first responders.

- ***Fails to Adequately Fund Port Security* —** The Homeland Security bill essentially freezes funding for port security grants at the 2004 level of $124 million, even though the Coast Guard reports needs in this area totaling $5.4 billion over ten years. The full Committee defeated a Democratic amendment that would have made additional funding available for port security grants which help ports install the fencing and other measures needed to prevent terrorists from gaining access to docks and other port facilities.

- ***Slashes Promised Conservation Funding*** — The 2005 Interior appropriations bill cuts funding for pressing conservation, recreation, and wildlife needs by nearly 22 percent below the 2004 enacted level. Congress committed to fund the Interior portion of the Conservation Trust Fund at $1.7 billion for 2005, yet the Interior appropriations bill provides only $832 million.

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June 1, 2004

Administration Confirms Its Plan to Cut Many Services Deeply in 2006

A White House memorandum dated May 19, 2004, confirms that the Administration's 2006 budget would impose deep cuts in many key government services. This memorandum contradicts earlier Administration denials of 2006 budget cuts buried deep within the unpublished budget numbers issued in February — cuts detailed in a February 19th House Budget Committee Democratic staff report. The May 19 Administration memorandum clearly directs agencies to "[a]ssume accounts are funded at the 2006 level specified in the 2005 Budget database" that shows the spending levels in the President's budget for agencies and programs for 2005 through 2009.

Hidden Long-Term Cuts in President's 2005 Budget — In its 2005 budget released in February, the Administration tried to cloak its cuts in 2006 through 2009. For the first time, the Administration excluded from its published budget materials the discretionary funding totals for programs and accounts beyond 2005. Only the Office of Management and Budget (OMB) computer tables show the budget's proposed funding — and cuts — for 2006 through 2009.

Agencies Cut in 2006, According to President's 2005 Budget
(billions of dollars of budget authority, OMB estimates)

	2005	2006	$ cut	% cut
Education	57.339	55.864	-1.475	-2.6%
Veterans Affairs	29.654	28.744	-0.910	-3.1%
EPA	7.759	7.609	-0.150	-1.9%
State	10.259	10.003	-0.256	-2.5%
Interior	10.849	10.605	-0.244	-2.2%
Social Security Administration	7.585	7.391	-0.194	-2.6%
National Science Foundation	5.745	5.628	-0.117	-2.0%
Small Business Administration	0.678	0.662	-0.016	-2.4%
Commerce	5.716	5.643	-0.073	-1.3%
Labor	11.880	11.676	-0.204	-1.7%
Health and Human Services	68.157	68.055	-0.102	-0.1%

White House Memo Contradicts Earlier Denials of Planned Cuts — In February, the Administration tried to repudiate the cuts in 2006 through 2009. OMB officials and at least one Cabinet Secretary said that the long-term estimates are calculated by formula and do not reflect policy decisions. However, the Administration's May 19 memo directs the agencies to abide by those totals for each budget account. Agencies may request higher figures for one or more of their accounts, but if so, they must offset those increases with decreases in their other accounts. In other words, if there is to be greater funding than in the Administration's 2005 budget for one education program, that increase must be offset by a cut in another education program.

Following are some examples of the planned cuts, for agencies and their programs, in the President's budget. These cuts come directly from the OMB database that shows the spending levels for 2005 through 2009.

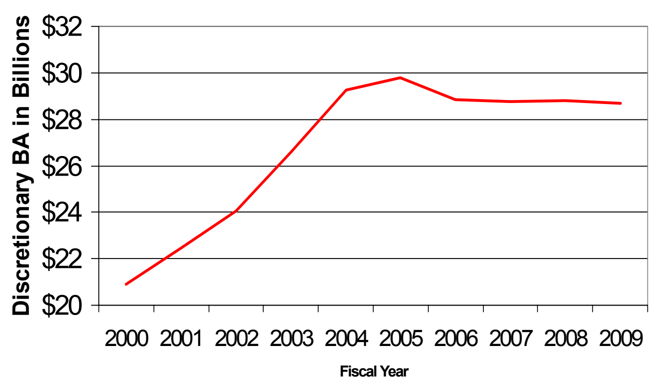
Cuts Department of Education Beginning in 2006

While the budget increases funding for the Department of Education by $1.7 billion from 2004 to 2005, it cuts the funding by $1.5 billion for 2006 and essentially freezes it at that low level for the following three years. Cuts for 2006 through 2009 will mean fewer children are challenged to learn and equipped to succeed, helped to meet the goals of the President's No Child Left Behind Act, or given assistance to afford and attend college.

- ***Shrinks Maximum Pell Grant Award*** — In the President's February budget, funding for Pell Grants would fall by $327 million for 2006, cutting the maximum award by at least $75 to a level below the 2002 maximum award, assuming that the cut to higher education is spread proportionally across programs.

Cuts Veterans Health Care

President's Budget Cuts Veterans' Appropriations Below 2004 Level



For 2006, the President's budget cuts funding for the Department of Veterans Affairs (VA) by $910 million (3.1 percent) below the 2005 requested level. And even that 2005 level was $1.2 billion less than what the Secretary of VA had originally requested. The Secretary also testified this spring that the funding levels for 2006 through 2009 in the President's budget may not be realistic. Over five years, the President's budget for appropriated veterans programs is $1.4 billion below a freeze at the 2004 enacted level. Almost all appropriated funding for veterans pays for medical care and hospital services. Future increases in health care prices and caseload will push VA medical funding needs well above a freeze at the 2004 level.

Cuts to Environmental Protection for 2005 and 2006

For 2005, the President's budget provides less than $7.8 billion in appropriations for the Environmental Protection Agency, a cut of nearly $600 million (7.0 percent) below the 2004 enacted level. For 2006, the Administration cuts EPA funding by an additional $150 million, providing only $7.6 billion. The Department of Interior will receive only $10.6 billion in 2006, a cut of $244 million (2.2 percent) below the proposed 2005 level. For 2005, the President's budget provides less than $4.0 billion for the Army Corps of Engineers, $597 million (13.1 percent) below the 2004 enacted level. For 2006, the Corps is cut by an additional $13 million.

Cuts National Science Foundation (NSF) in 2006 and Beyond

While the President's budget increases funding for NSF by $167 million for 2005, it then cuts it by $117 million in 2006. In the five years of the President's budget, NSF never again reaches the 2005 level of funding.

Cuts Department of Commerce in 2006

Despite a net loss (as of June 1) of 2.2 million private-sector jobs since the Bush Administration took office, the President's budget cuts appropriations for the Department of Commerce by 1.3 percent from 2005 to 2006.

- ***Shrinking Support for International Trade Administration (ITA)*** — The ITA assists in the creation of U.S. jobs by aiding the growth of export businesses, enforcing U.S. trade laws and agreements, and improving access to overseas markets by pressing for the removal of trade barriers. The budget highlights its $12 million increase for ITA, for a 2005 total of $394 million, but then follows this with a $10 million reduction for 2006 and virtually no growth thereafter.

Cuts Department of Labor Beginning in 2006

For 2006, the President's budget cuts appropriations for the Department of Labor to a level that is below even the 2004 enacted level of $11.7 billion. To reach that agency level, the President's budget cuts job training. For 2005, the budget essentially freezes funding for training and employment programs at $5.9 billion, although within that total, the budget cuts existing adult training and dislocated worker programs by $151 million. For the next four years, the budget cuts total funding below the 2005 amount, with the steepest cut in 2006. This cut in job training comes even though the economy has lost millions of jobs since President Bush took office and an increasing number of jobs are being sent overseas.

Cuts Health and Human Services in 2006

The President's budget cuts funding for the Department of Health and Human Services by $102 million for 2006. To achieve that cut, the budget cuts appropriations both for programs that help children and for agencies that support health research.

- ***Eliminates Child Care for Nearly Half a Million Children* —** For 2006, the President's budget cuts funding for the Child Care and Development Block Grant by $53 million below the 2005 level, and for the next three years it cuts funding below the 2004 level. Federal resources for child care also include the Child Care Entitlement to States (which the budget freezes at $2.7 million through 2009), as well as TANF and Social Services Block Grant funds spent on child care at state discretion. Considering all funding available for child care, the budget projects that the number of children receiving assistance will decline from 2.5 million in 2003 to 2.2 million in 2009. Independent experts estimate that the loss under the President's budget will be even worse, eliminating child care for 447,000 children. Meanwhile, the President's plan to increase work requirements for welfare recipients will increase the demand for affordable child care.

- ***Cuts Funding for Head Start After 2005*** — The President provides sufficient funding to freeze Head Start enrollment for 2005, but then reduces funding in the following years, cutting $177 million (2.5 percent) for 2006, assuming that the cut to children and family programs is applied across the board. Head Start currently serves less than 60 percent of eligible four-year-olds, but these cuts would mean even fewer children would be able to attend Head Start.

- ***National Institutes of Health (NIH) Increase in 2005 is Reversed in 2006* —** After providing average annual growth of nearly 15 percent from 1998 to 2003 — doubling NIH's budget — the 2005 budget holds NIH funding to its lowest increase in years. The budget provides $28.6 billion for NIH, an increase of $711 million (2.6 percent) over the 2004 enacted level. The budget then cuts NIH by 2.1 percent for 2006, and provides minuscule increases for subsequent years. At no time over the five-year period does NIH funding again reach the 2005 level.

- ***Health Resources and Services Administration (HRSA) Cut Two Years in a Row*** — The mission of HRSA is to "improve and expand access to quality health care for all," and its programs include community health centers, rural health programs, access to health care for people living with HIV/AIDS, and training and recruitment of health care professionals, to name a few. In 2005, the budget provides $6 billion, a cut of $638 million below the 2004 enacted level. The budget then cuts HRSA even further for 2006, this time providing $785 million less than the 2004 level.

Conclusion

The May 19 White House memorandum confirms that the Administration does plan to cut key government services next year, including some it brags about increasing this year. The Administration is requiring these cuts because it chose to promote oversized tax cuts, and now cannot afford to fund vital government services.

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July 21, 2004

Inflation and Stagnant Wages Leave Low- and Middle-income Workers Behind

Dear Democratic Colleague:

There is growing evidence that little benefit from Bush Administration economic policies is trickling down to average working Americans. As prices rise for fuel, food, and other necessities, wages remain flat. June data from the Bureau of Labor Statistics shows that average hourly earnings for production and non-managerial workers declined by 1.1 percent between June 2003 and June 2004, after accounting for inflation. I commend to you the attached articles from *The New York Times* and *The Wall Street Journal* , published July 18 and July 20, respectively, which describe the struggle that low-wage and middle-income families face in the current economic environment.

Sincerely,
/s
John M. Spratt, Jr.
Ranking Democratic Member

The New York Times

July 18, 2004

Hourly Pay in U.S. Not Keeping Pace With Price Rises

By EDUARDO PORTER

The amount of money workers receive in their paychecks is failing to keep up with inflation. Though wages should recover if businesses continue to hire, three years of job losses have left a large worker surplus.

"There's too much slack in the labor market to generate any pressure on wage growth," said Jared Bernstein, an economist at the Economic Policy Institute, a liberal research institution based in Washington. "We are going to need a much lower unemployment rate." He noted that at 5.6 percent, the national unemployment rate is still back at the same level as at the end of the recession in November 2001.

Even though the economy has been adding hundreds of thousands of jobs almost every month this year, stagnant wages could put a dent in the prospects for economic growth, some economists say. If incomes continue to lag behind the increase in prices, it may hinder the ability of ordinary workers to spend money at a healthy clip, undermining one of the pillars of the expansion so far.

Declining wages are likely to play a prominent role in the current presidential campaign. Growing employment has lifted President Bush's job approval ratings on the economy of late. According to the latest New York Times/CBS News poll, in mid-July, 42 percent of those polled approved of the president's handling of the economy, up from 38 percent in mid-March.

Yet Senator John Kerry, the likely Democratic presidential nominee, is pointing to lackluster wages as a telling weakness in the administration's economic track record. ``Americans feel squeezed between prices that are rising and incomes that are not," Mark Mellman, a pollster for the campaign, said in a memorandum last month.

On Friday, the Bureau of Labor Statistics reported that hourly earnings of production workers - nonmanagement workers ranging from nurses and teachers to hamburger flippers and assembly-line workers - fell 1.1 percent in June, after accounting for inflation. The June drop, the steepest decline since the depths of recession in mid-1991, came after a 0.8 percent fall in real hourly earnings in May.

Coming on top of a 12-minute drop in the average workweek, the decline in the hourly rate last month cut deeply into workers' pay. In June, production workers took home $525.84 a week, on average. After accounting for inflation, this is about $8 less than they were pocketing last January, and is the lowest level of weekly pay since October 2001.

On its own, the decline in workers' wages is unlikely to derail the recovery. Though they account for some 80 percent of the work force, they contribute much less to spending. Mark M. Zandi, chief economist at Economy.com, a research firm, noted that households in the bottom half of income distribution account for only one-third of consumer spending.

Nonetheless, coming after the bonanza of the second half of the 1990's, the first period of sustained real wage growth since the 1970's, the current slide in earnings is a big blow for the lower middle class. Moreover, the absence of lower income households could also weigh on overall economic growth - putting a lid on the mass market and skewing consumption toward high-end products.

"There's a bit of a dichotomy," said Ethan S. Harris, chief economist at Lehman Brothers. "Joe Six-Pack is under a lot of pressure. He got a lousy raise; he's paying more for gasoline and milk. He's not doing that great. But proprietors' income is up. Profits are up. Home values are up. Middle-income and upper-income people are looking pretty good."

Tales of tight budgets at the bottom are springing up across the country. "I haven't had a salary increase in two years, but the cost of living is going up," said Eric Lambert, 42, a father of three who earns $13 an hour as a security guard at 660 Madison Ave. in Manhattan.

Silvia Vides, 43, who earns $11 an hour in a union job as a housekeeper at the Universal City Sheraton hotel in Los Angeles, said, "Sometimes I don't know how I pay the bills and food and rent." She has cut back on all nonessential expenditures and she is four months behind on payments on $4,000 in credit-card debt.

Their woes are a product of supply and demand for labor. From 1996 through 2000 when employers were hiring hand over fist, real hourly wages of ordinary workers rose by 7.5 percent. Those for leisure and hospitality workers rose 9.6 percent, and retail workers' climbed 8.9 percent. The raises continued even as the economy slipped into recession in 2001 and businesses began to shed workers.

From 2001 to 2003, 2.4 million jobs were eliminated, as businesses sharply reduced their work forces, refusing to hire back even as demand started picking up. Over a million of these jobs have been regained this year.

Yet with the lowest number of people employed as a share of the population since 1994, there is still a plentiful supply of unused laborers looking for jobs.

As the rise in energy prices in the earlier months of this year led to rising inflation, pushing prices in June up 3.2 percent from the same month of last year, the lackluster job market has left workers in a weak position to demand more money.

"Since last November, we've had a pickup in hiring and a pickup in hours worked in virtually all of our businesses," said David Pittaway, a senior managing director at Castle Harlan, an equity investment company that owns everything from Burger King franchises to a shipping company.

But there is clearly still a lot of slack. When Castle Harlan advertised in the newspapers to fill 70 to 80 positions at a Morton's restaurant it opened in early July in White Plains, 600 to 700 people showed up.

Ms. Vides in California ticks off the items of a rising cost of living. She pays $850 a month for a one-bedroom apartment in Panorama City, $25 more a month than last year. The cost of a bus pass rose $10, to $45 a month. The electricity bill is much higher and food costs more. "I've got to do miracles with my salary," she said.

So Ms. Vides said she was outraged that the hotels negotiating a new contract with her union were offering annual raises of 40 cents to 45 cents an hour each year for the next five years. The raise in 2004 would be about 4 percent, just enough to keep up with the 4 percent rise in prices in Los Angeles over the last year. "This is miserly," said Ms. Vides, who said the union wants $1.25 this year and $1.50 next.

Colleen Kareti, president of the Los Angeles hotel employers' council, which represents the hotels, argued that negotiations had not yet gotten down to bargaining over wages. But she pointed out that times are hard for the hotel business, too. "It's been pretty bad for the last three years. We're nowhere near the levels of business where we were in 1998 through 2000," Ms. Kareti said.

Some economists warn that if wages remain depressed for a long time they may end up weighing on the economy. "The recovery will likely continue on despite the travails of lower-income households, but it cannot flourish," Mr. Zandi said.

So far, spending has been fueled mostly by debt, as consumers took advantage of bedrock-low interest rates to whip out their credit cards and refinance their mortgages. But as interest rates rise to keep inflation in check, continued growth in consumer spending will depend more on jobs and wages.

Spending is still holding up, led by strong corporate profits as well as higher salaries and bonuses at the upper end of the income distribution. But the lagging earnings at the bottom end are making for a somewhat lopsided expansion.

The upper echelons of consumer spending, at places like Saks Fifth Avenue, Neiman Marcus and Nordstrom department stores, are reporting gangbuster business. "I'm surprised by how well we've sold high-priced fashion at this stage," said Pete Nordstrom, president of Nordstrom's full-line stores.

But at the other end, sales at stores open at least a year at big-box discounters like Target and Wal-Mart have disappointed, while sales of used cars are declining year over year, government figures show. "We're not seeing the traffic, not even the same volumes of sales calls," said Richard Cooper, a sales manager at Jones Ford in Charleston, S.C.

Wages at the bottom should eventually recover, as businesses continue hiring to meet growing demand. The question is how fast. "As unemployment slides down, more of the benefits of growth should flow to the working class," Mr. Bernstein said. "But not until we reach truly full employment are they likely to see their earnings rise at a level closer to that of productivity."

The Wall Street Journal

So Far, Economic Recovery Tilts To Highest-Income Americans

They Gain More, Spend More; With Job Market Rising, Will Others Feel Rebound?

Mr. Williams Waits for a Raise

By JON E. HILSENRATH and SHOLNN FREEMAN
Staff Reporters of THE WALL STREET JOURNAL
July 20, 2004; Page A1

Joshua Berry and Ricky Williams, both Houstonians, have seen two very different economic recoveries.

Mr. Berry, an entrepreneur, has profited handsomely from the stock market, in the real-estate boom and by selling a business. Mr. Williams, an airline baggage handler, has been waiting since 2001 for a pay raise.

With the U.S. economy expanding and the labor market improving, it isn't clear how well the Democrats' message of a divided America will resonate with voters this fall. But many economists believe the economic recovery has indeed taken two tracks, exemplified by the experiences of these two Texas residents.

Upper-income families, who pay the most in taxes and reaped the largest gains from the tax cuts President Bush championed, drove a surge of consumer spending a year ago that helped to rev up the recovery. Wealthier households also have been big beneficiaries of the stronger stock market, higher corporate profits, bigger dividend payments and the boom in housing.

Lower- and middle-income households have benefited from some of these trends, but not nearly as much. For them, paychecks and day-to-day living expenses have a much bigger effect. Many have been squeezed, with wages under pressure and with gasoline and food prices higher. The resulting two-tier recovery is showing up in vivid detail in the way Americans are spending money.

Hotel revenue was up 11% in the first five months of 2004 at luxury and upscale chains, but up just 3% at economy chains, according to Smith Travel Research, a market-research firm. At the five-star Broadmoor Hotel in Colorado Springs, Colo., $600-a-night lakeside suites are sold out every day through mid-October.

At high-end Bulgari stores, meanwhile, consumers are gobbling up $5,000 Astrale gold and diamond "cocktail" rings made for the right hand, a spokeswoman says. The Italian company's U.S. revenue was up 22% in the first quarter. Neiman Marcus Group Inc., flourishing on sales of pricey items like $500 Manolo Blahnik shoes, had a 13.5% year-over-year sales rise at stores open at least a year.

By contrast, such "same store" sales at Wal-Mart Stores Inc., retailer for the masses, were up just 2.2% in June. Wal-Mart believes higher gasoline costs are pinching its customers. At Payless ShoeSource Inc., which sells items like $10.99 pumps, June same-store sales were 1% below a year earlier.

A similar pattern shows up in cars. Luxury brands like BMW, Cadillac and Lexus saw double-digit U.S. sales increases in June from a year earlier. Sales of lower-tier brands such as Dodge, Pontiac and Mercury either declined or grew in the low single digits.

"To date, the [recovery's] primary beneficiaries have been upper-income households," concludes Dean Maki, a J.P. Morgan Chase (and former Federal Reserve) economist who has studied the ways that changes in wealth affect spending. In research he sent to clients this month, Mr. Maki said, "Two of the main factors supporting spending over the past year, tax cuts and increases in [stock] wealth, have sharply benefited upper income households relative to others."

The good times upper-income Americans are enjoying represent a bounce-back from the hit that many of the wealthiest took after bonus income dried up in 2001 and 2002 and stock options went sour. For example, Wall Street compensation was up 16% in the first quarter from a year earlier, after having fallen from stratospheric levels the three previous years, according to the Securities Industry Association.

Longer-term issues are also at work. Wage and income disparities between the rich and poor have generally been widening for nearly 20 years. In 1980, the top 10% of households in income accounted for 33% of total household income, according to economist Emmanuel Saez at University of California, Berkeley. By 2000, that had risen to 44%. The figures exclude capital gains. Mr. Saez says the concentration of income at the top dropped during the recession but has probably started picking up again.

Some economists believe the gap is driven wider by technological change and by the economy's increasing openness to global competition. Technology rewards skilled workers, and competition has generally punished the unskilled, who are susceptible to the movement of work overseas. Both factors have come into play in recent years as technology-driven productivity surged and the U.S. trade deficit widened.

Meanwhile, the U.S. has seen a big increase in the sheer number of affluent families. In 2002, nearly 16 million U.S. households had annual incomes of more than $100,000, up from a little more than five million 20 years ago, in inflation-adjusted terms.

For a sense of the divide, contrast the recovery experiences of Mr. Berry, a businessman who earns a six-figure income, and Mr. Williams, the baggage handler, who makes around $20 an hour for Southwest Airlines. Both have been shopping this month at the River Oaks Chrysler-Jeep car dealership in Houston.

Mr. Berry, 34 years old, is president of a nurse staffing business called ShiftBay.com. Last year, he and some partners sold a medical-supply business. Mr. Berry says that together they saved more than $100,000 in taxes, thanks to a reduction last year in the federal income-tax rate on long-term capital gains.

Mr. Berry also is in the process of selling his house, which he says has appreciated by almost $100,000 over four years. And he says that while he lost a lot of money in the stock-market downturn that began four years ago, he has enjoyed hefty gains since the market turned up about 15 months ago. Mr. Berry is choosing between sticking with Chrysler (he now drives a Jeep Grand Cherokee) or trading up to a Cadillac, BMW or Mercedes-Benz.

Mr. Williams, 52, hasn't benefited from the boom in the price of houses because he doesn't own one. His pay hasn't budged since 2001, although he is expecting a raise this month. Within a year, he expects his hourly pay to rise to about $24.

Mr. Williams's car lease (he, too, drives a Grand Cherokee) will be up in October, and he has been scrambling to come up with a down payment for a new Chrysler PT Cruiser. He was still $1,800 short last week. A Chrysler salesman was able to make up part of the difference with an additional $1,000 rebate targeted at returning lease customers, on top of $4,000 in manufacturer's incentives already on the table.

"With the economy the way it is, I've had to rob Peter to pay Paul, and then sometimes rob them both," Mr. Williams says.

The perception of a fast-lane/slow-lane recovery has become a central political issue. This year's stronger job market has led Democrats to shift their emphasis: away from the argument that Bush policies have failed to produce jobs and toward the idea that the expansion's fruits haven't been widely shared.

"They're telling people this is the best economy we've had," Sen. John Kerry mockingly told a riverbank crowd last Thursday evening in Charleston, W.Va., drawing jeers. "What does it mean when you don't have any health care at all?" Hands started popping up throughout the audience, as Mr. Kerry paused to point to each one. "Too many people in Washington have no sense at all about what's happening," he said. His running mate, Sen. John Edwards, speaks of "Two Americas," one "that does the work, another America that reaps the rewards."

Bush critics have argued that the economy is producing jobs mainly in low-paying industries like restaurants and temporary work. Mr. Bush counters that his opponents have been pessimistically distorting the economic statistics, ignoring the gains. The Bush campaign cites data from the Bureau of Labor Statistics showing that in the past year, there has been more net employment growth in occupations with above-average pay than in occupations with below-average pay.

Campaigning in Wisconsin last week, Mr. Bush spoke of a local family of six who benefited from elements of his tax package aimed at lower- and middle-income families, such as the child tax credit. "Oh, some of the sophisticates will say that $2,700 doesn't matter to the Muellers: 'It doesn't sound like a lot to me,' " Mr. Bush said. "It is a lot to them. That's what counts."

Polls suggest that Americans aren't giving the president full credit for an economic recovery, and the class divide in this recovery may help explain that. A Wall Street Journal/NBC News poll in late June found that 45% of Americans approved of his handling of the economy, while 49% didn't.

Mr. Maki of J.P. Morgan Chase estimates that in terms of dollars saved, the top 20% of households by income got 77% of the benefit of the 2003 tax cuts, and roughly 50% of the 2001 tax cuts. And of stocks held by households, roughly 75% are owned by the top 20% of those households. That made them prime beneficiaries of last year's stock-market rally, although also big sufferers from the stock carnage from 2000 to 2002.

The affluent also benefit more from stock dividends, on which the federal income-tax rate was cut last year retroactive to the start of 2003. Total dividend payments have risen 11% to $3 billion since the end of 2002, estimates Berkeley's Mr. Saez. Higher-income households also are larger beneficiaries of the surge in corporate earnings, which helps to drive dividend and stock returns. The level of corporate profits has risen 42% since the last recession, which ended in the final quarter of 2001. Wage and salary income is up just 6.3% in that time. Meanwhile, housing values have appreciated fastest in the most affluent regions during the past three years, according to research by Fiserv CSW Inc., which tracks home prices.

Many economists say the lopsided recovery is now at a critical juncture. The impetus from new tax cuts has largely passed, and the stock market has lost momentum, two factors that could slow the pace of higher-income people's spending in the months ahead. As a result, the time has come for the recovery either to broaden out to more-modest income groups -- or possibly lose momentum.

The late 1990s showed that lower-wage workers benefit when unemployment falls, as the tighter labor market helps underpin wages across income categories. With the job market improving, there is a chance this could happen again, but the outlook is still highly uncertain. Payroll employment has increased by 1.5 million since last August. And some companies that cater to the mass market say they have noticed the turnaround. "We had a terrific Fourth of July weekend," says Wayne Wielgus, a senior vice president at Choice Hotels International Inc., which serves low- and middle-income travelers with brands like EconoLodge and Comfort Inn.

But some economists worry that the early stage of the recovery for low- to middle-income families is being squeezed by continuing pressure on wages and purchasing power. Average hourly earnings have risen at just a 1.9% annual rate since the job market started improving notably last August. Meanwhile, the consumer-price index -- driven by higher food and gasoline prices -- has risen at a 3.3% annual pace. The average worker's purchasing power, in other words, has declined even as more people have been finding jobs since August.

Weekly earnings for production workers and nonsupervisors at service companies, adjusted for inflation, were down 2.6% in June from a year earlier. This slip might be transitory, and it wasn't anywhere near the drops of 5% to 7.5% registered in the late 1970s and early 1980s. Still, it was the largest decline since 1991, and it is a shift from the late 1990s and even the 2001 recession, when real wages were increasing.

As a result, after rising last year, the University of Michigan's consumer confidence index for lower-income households is off 12% so far this year. Confidence among the affluent is lower as well, but by a smaller 6.7%.

The recovering job market and an easing of food- and gasoline-price increases could reverse some of today's pressures. But these aren't the only issues hanging over lower-income households. Many are also highly exposed to rising interest rates, says Mark Zandi, chief economist at Economy.com, because these households were more likely to take out adjustable-rate mortgages to squeeze into an ever-pricier housing market. For those who don't own homes, the chances of buying have become more remote as house prices have soared. "Lower- and middle-income groups are going to remain under significant pressure," Mr. Zandi says.

Many in this group are also getting squeezed as health-care costs rise and companies seek to shift the burden to workers. From 2000 to 2003, employees' average annual out-of-pocket expenses for family medical premiums rose 49% to $2,412, according to an employer survey by Kaiser Family Foundation, a nonprofit research group in Menlo Park, Calif.

Becky Salas, a 32-year-old vocational nurse in San Antonio, says her family is still pinching pennies, even though she believes an economic recovery is taking hold now. Two years ago, she and her husband stopped using credit cards. Expensive toys for her children, movies at theaters and meals at McDonald's also are out. "Easily we could spend $20 at McDonald's for just one meal," Ms. Salas says. And "we can go fly a kite, instead of going to an expensive theater where the kids are going to yell and scream and won't enjoy it anyway."

Solved! The Mystery of the Missing Mid-Session Review

Republican Budget To Do List

- ☑ Set a new deficit record
- ☐ Deliver Mid-Session Review on time
- ☐ Pass a budget resolution conference report
- ☐ Pass a debt ceiling increase
- ☐ Pass effective PAYGO extension, spending caps
- ☐ Pass appropriations conference reports on time

Mid-Session Review Must Be Submitted By July 15

Chapter 11 of Title 31 U.S. Code
§ 1106. Supplemental budget estimates and changes

(a) ***Before July 16 of each year, the President shall*** submit to Congress a supplemental summary of the budget for the fiscal year for which the budget is submitted under section 1105(a) of this title. This summary shall include ---

(1) for that fiscal year ---

(A) substantial changes in or reappraisals of estimates of expenditures and receipts;

(B) substantial obligations imposed on the budget after its submission;

(C) current information on matters referred to section 1105 (a)(8) and (9)(B) and (C) of this title; and

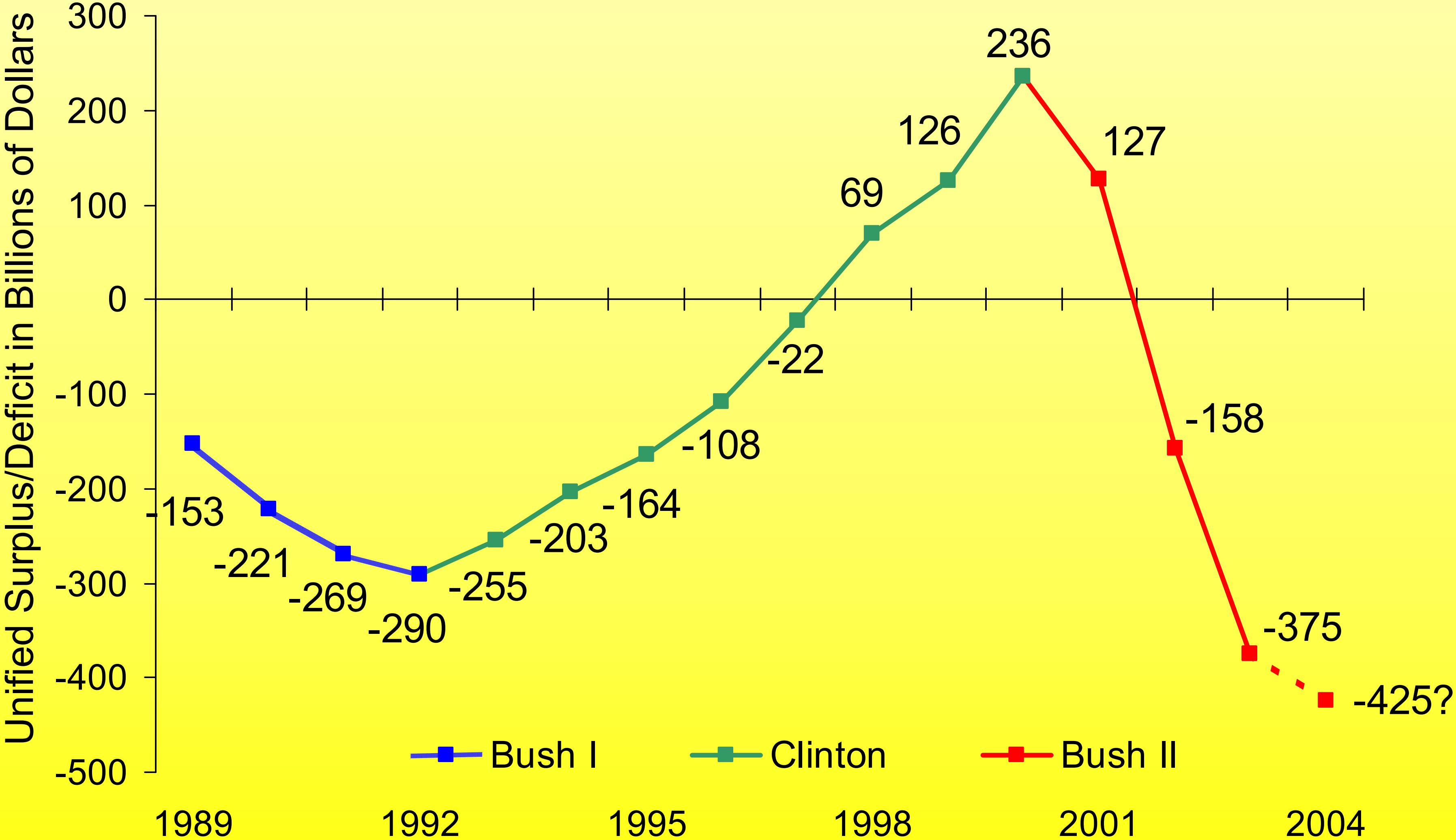
(D) additional information the President decides is advisable to provide Congress with complete and current information about the budget and current estimates of the functions, obligations, requirements, and financial condition of the United States Government;

(2) for the 4 fiscal years following the fiscal year for which the budget is submitted, information on estimated expenditures for programs authorized to continue in future years, or that are considered mandatory, under law; and

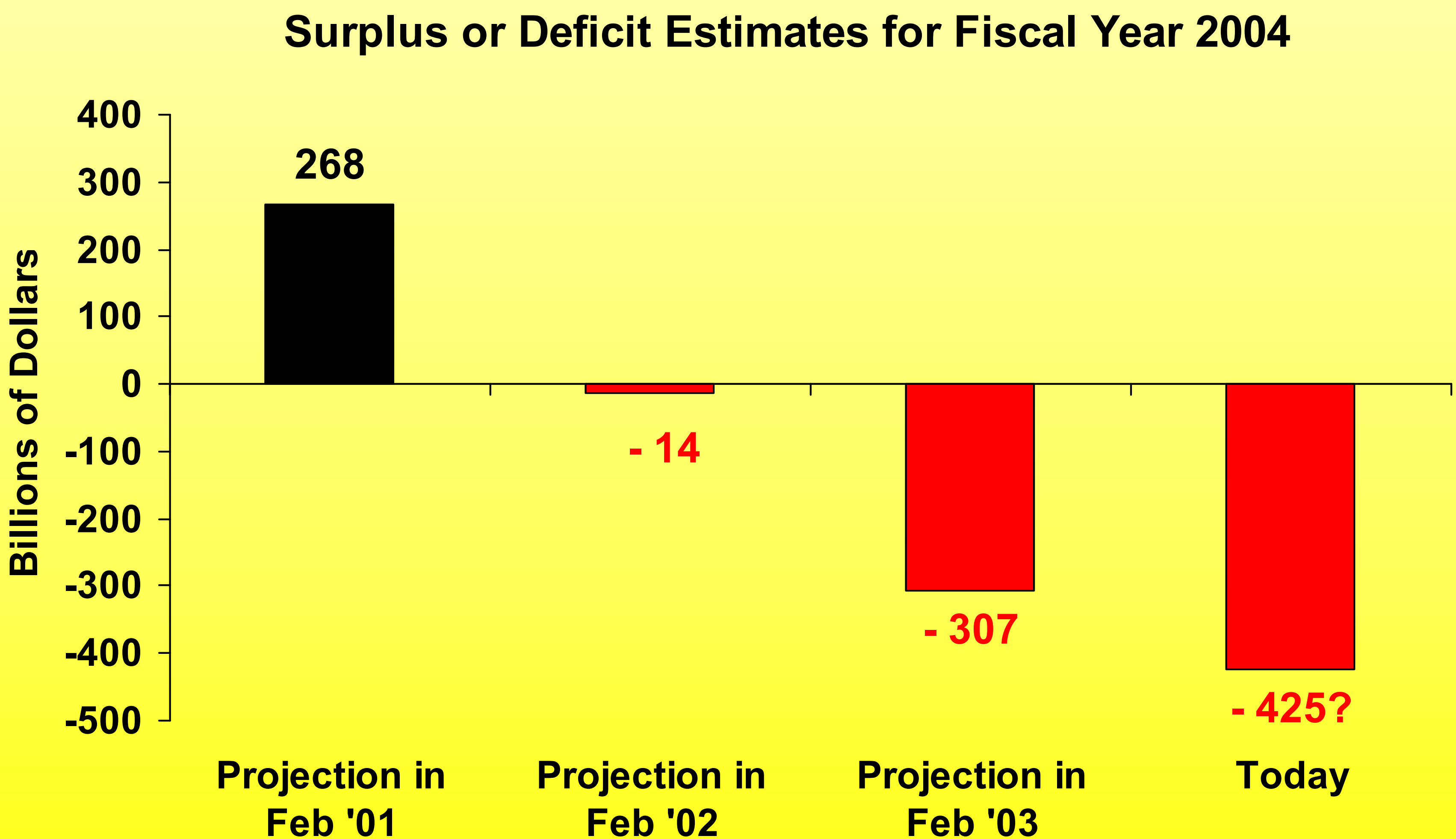
(3) for future fiscal years, information on estimated expenditures of balances carried over from the fiscal year for which the budget is submitted.

Backsliding Into the Deficit Ditch

From Deficit to Surplus to Deficit Again

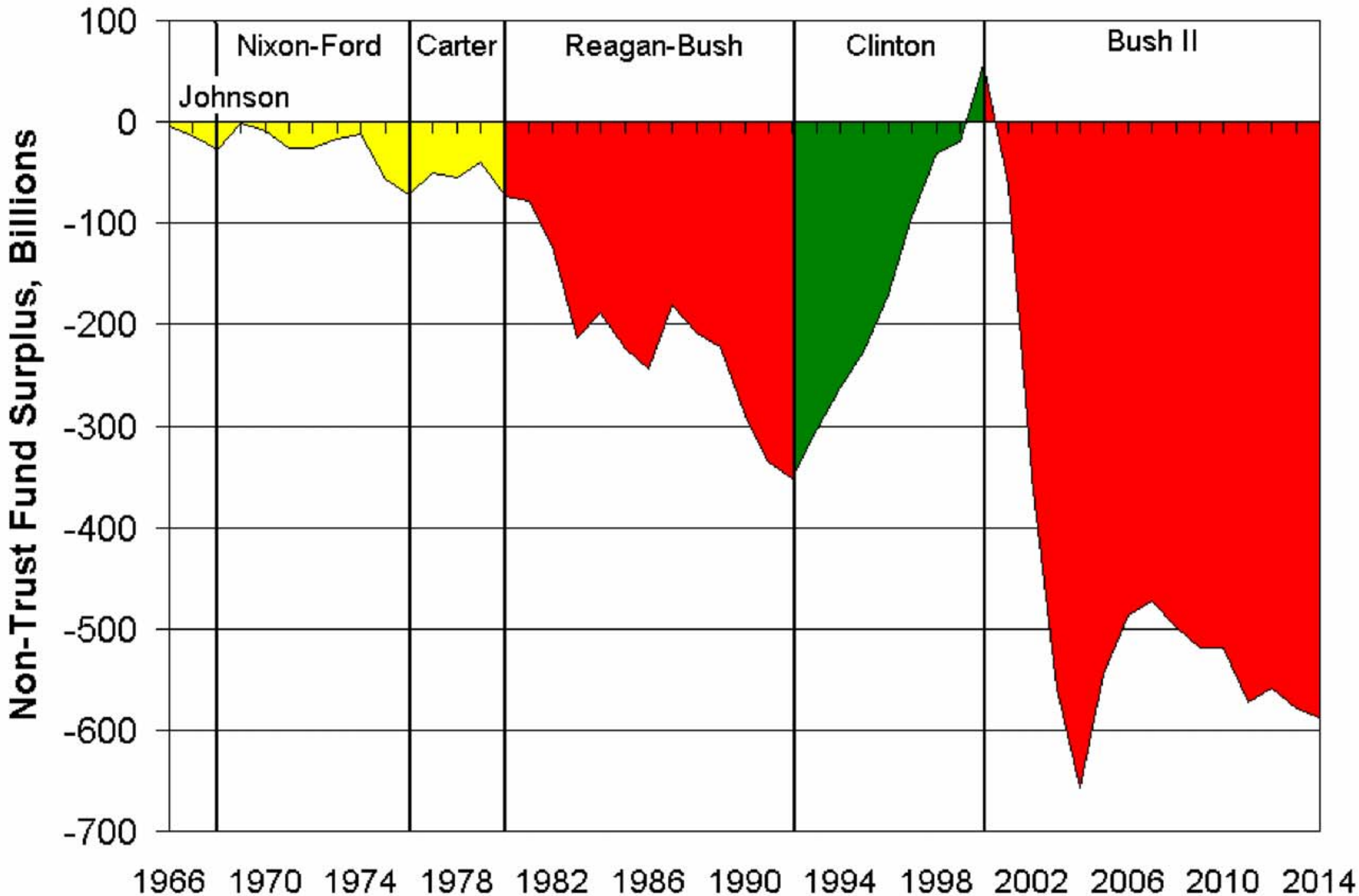


With New OMB Estimates, 2004 Budget Gets Worse



A Fiscal Opportunity Lost

Total Surplus or Deficit without Social Security or Medicare Trust Fund Surpluses



Prepared by the House Budget Committee Democratic Staff Source: CBO 3/1/04

OMB Estimates Won't Tell the Whole Story About the Deficit

OMB's estimates omit:

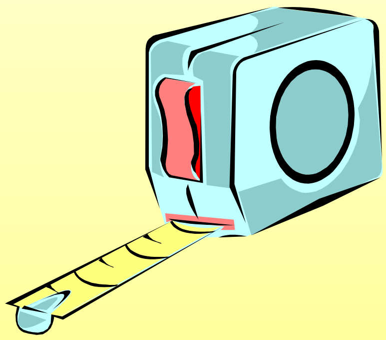
- Exploding tax cuts after 2010;
- Needed middle-income AMT relief;
- Realistic costs of military operations in Iraq and Afghanistan; and
- Resulting debt-service costs.

Fiscal Report Card

Republican Budget Failures

- __F__ No Mid-Session Review
- __F__ No budget resolution conference report
- __F__ No debt ceiling increase
- __F__ No effective PAYGO rules or spending caps
- __F__ No completed appropriations bills
- __F__ Record-high deficits

2004 Deficit Will Be About $425 Billion



- **The largest deficit in American history**
- $50 billion worse than last year's $375 billion
- $675 billion worse than the Administration projected in 2001
- $600 billion if the Social Security surplus is not counted
- 4% of the GDP, or 5% not counting the Social Security surplus
- $40 billion greater than all non-homeland security domestic discretionary spending
- Only $25 billion less than all defense spending
- 55% as large as all individual income taxes
- 85% as large as all Social Security benefits
- 45% more than all Medicare spending